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FINANCIAL SERVICES COMPETITION  
ACT OF 1997

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SUPPLEMENTAL REPORT

OF THE

COMMITTEE ON  
BANKING AND FINANCIAL SERVICES  
HOUSE OF REPRESENTATIVES

ON

H.R. 10

[Including cost estimate of the Congressional Budget Office]



SEPTEMBER 17, 1997—Ordered to be printed

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**LETTER OF SUBMITTAL**

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HOUSE OF REPRESENTATIVES,  
COMMITTEE ON BANKING AND FINANCIAL SERVICES,  
*Washington, DC, September 17, 1997.*

Hon. NEWT GINGRICH,  
*Speaker, House of Representatives,*  
*The Capitol, Washington, DC.*

DEAR MR. SPEAKER: On behalf of the Committee on Banking and Financial Services, I am transmitting herewith a supplemental report to accompany the bill, H.R. 10, the Financial Service Competition Act of 1997.

Sincerely,

JAMES A. LEACH, *Chairman.*

FINANCIAL SERVICES COMPETITION ACT OF 1997

SEPTEMBER 17, 1997.—Ordered to be printed

Mr. LEACH, from the Committee on Banking and Financial Services, submitted the following

SUPPLEMENTAL REPORT

[To accompany H.R. 10]

[Including cost estimate of the Congressional Budget Office]

U.S. CONGRESS,  
CONGRESSIONAL BUDGET OFFICE,  
*Washington, DC, September 12, 1997.*

Hon. JAMES A. LEACH,  
*Chairman, Committee on Banking and Financial Services, House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the two enclosed cost estimates the H.R. 10, the Financial Services Competition Act of 1997. One estimate includes federal costs and the state and local impact. The other estimate covers the private-sector impact.

If you wish further details on these estimates, we will be pleased to provide them. The CBO staff contacts are Mary Maginniss (for federal costs); Mark Booth (for federal revenues); Marc Nicole (for the state and local impact); and Patrice Gordon and Judith Ruud (for the private-sector impact).

Sincerely,

JAMES L. BLUM  
(For June E. O'Neill, Director).

Enclosures.

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

*H.R. 10—Financial Services Competition Act of 1997*

Summary: H.R. 10 would abolish the federal thrift charter, thus allowing the merger of the bank and thrift insurance funds, and would eliminate certain barriers to ties between insured depository

institutions and other financial and commercial firms. While these changes could affect the government's spending for deposit insurance, CBO has no basis for predicting whether the long-run costs of deposit insurance would be higher or lower than under current law. Because insured depository institutions pay premiums to cover these costs, any such changes would have little or no impact on the budget over time. CBO estimates that implementing the bill would increase other direct spending \$4 million in 1998 and \$62 million over the 1998–2002 period, and would decrease revenues by \$1 million in 1998 and \$17 million over the 1998–2002 period. Assuming appropriation of the necessary amounts, CBO estimates that several agencies would spend between \$3 million and \$4 million annually to carry out the provisions of the bill, once fully implemented. Because H.R. 10 would affect direct spending and receipts, pay-as-you-go procedures would apply.

H.R. 10 contains several intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA), but CBO estimates that the costs of complying with these mandates would total less than \$10 million annually and thus would not exceed the threshold established under that act (\$50 million in 1996, adjusted annually for inflation). H.R. 10 also contains several private-sector mandates as defined in UMRA. CBO's estimate of the cost of those private-sector mandates is detailed in a separate statement.

Description of the bill's major provisions: H.R. 10 would:

- Require all federally chartered savings associations to convert to a national bank or state charter within two years after date of enactment, merge the Office of Thrift Supervision (OTS) with the Office of the Comptroller of the Currency (OCC), and allow the merger of the Savings Association Insurance Fund (SAIF) and the Bank Insurance Fund (BIF);

- Permit affiliations of banking, securities, and insurance companies;

- With certain revenue limitations, allow non-banking commercial firms to own small banks through a well-capitalized holding company and allow bank holding companies to own commercial firms;

- Provide for a new type of wholesale financial institution that does not accept retail insured deposits, known as a "wooffie";

- Create a 10-member National Council on Financial Services (NCFS), comprising representatives from state and federal regulatory agencies; the NCFS would determine which products offered by banks and other providers of financial services are financial in nature, would identify the appropriate regulator for these products, and would regulate disputes involving the definition of these products;

- Reform the Federal Home Loan Bank (FHLB) System, making membership voluntary; limit FHLBs' investments only to those necessary for liquidity, safety and soundness, and housing finance; and replace the \$300 million annual payment made by the FHLBs for interest on bonds issued by the Resolution Funding Corporation (REFCORP) with an assessment set at 20.75 percent of the FHLBs' net income;

Require insured depository institutions and their subsidiaries to adopt a number of consumer protection measures affecting sales of nondeposit products.

Require the General Accounting Office (GAO) to report annually on market concentration in the financial services industry;

Amend the Securities Exchange Act of 1934 to define bank employees or bank affiliates as “brokers” if they conduct certain activities; and

Shift from the financial regulatory agencies to the Department of Justice (DOJ) the authority to review the competitive effects of the antitrust laws involving mergers of depository institutions.

Estimated cost to the Federal Government: H.R. 10 would make a number of changes affecting direct spending and revenues, which would result in increased spending by the banking regulatory agencies and the FHLBs, and a decrease in the annual payment—recorded as revenues—that the Federal Reserve remits to the Treasury. CBO estimates that direct spending would increase by about \$62 million over the 1998–2002 period. We estimate that enacting H.R. 10 would decrease revenues by \$17 million over the same period. The bill also would increase discretionary spending by an estimated \$14 million over the 1998–2002 period, assuming appropriation of the necessary amounts. The estimated budgetary impact of H.R. 10 is shown in the following table.

The budgetary effects of this legislation on outlays fall within budget functions 370 (commerce and housing credit) and 900 (interest). The legislation would also affect revenues (governmental receipts).

*Basis of estimate*

*Direct spending and revenues*

H.R. 10 could affect direct spending for deposit insurance by increasing or decreasing amounts paid by the insurance funds to resolve insolvent institutions and to cover the administrative expenses necessary to implement its provisions. Changes in spending related to failed banks and thrifts could be volatile and vary in size from year to year, but any such costs would be offset by insurance premiums, and thus their budgetary impact would be negligible over time. The bank regulators would also incur expenses related to the proposed legislation, but not all of these costs would be offset by fees. The contribution the FHLBs make to pay interest on REFCORP bonds would increase, thus reducing the Treasury payment to REFCORP. Finally, H.R. 10 also would affect revenues by reducing annual payments from the Federal Reserve to the Treasury.

	By fiscal years, in millions of dollars—					
	1997	1998	1999	2000	2001	2002
DIRECT SPENDING						
Spending Under Current Law: <sup>1</sup>						
Estimated Budget Authority .....	2,328	2,328	2,328	2,328	2,328	2,328
Estimated Outlays .....	-10,152	-1,934	-526	1,160	1,845	2,038
Proposed Changes:						
Estimated Budget Authority .....	0	0	-22	-17	-4	-1

	By fiscal years, in millions of dollars—					
	1997	1998	1999	2000	2001	2002
Estimated Outlays .....	0	4	8	11	18	21
Spending Under H.R. 10 <sup>1</sup>						
Estimated Budget Authority .....	2,328	2,328	2,306	2,311	2,324	2,327
Estimated Outlays .....	-10,152	-1,930	-518	1,171	1,863	2,059
CHANGES IN REVENUES						
Estimated Revenues <sup>2</sup> .....	0	-1	-4	-4	-4	-4
CHANGES IN SPENDING SUBJECT TO APPROPRIATION						
Estimated Authorization Level .....	0	1	3	3	3	4
Estimated Outlays .....	0	1	3	3	3	4

<sup>1</sup> Includes spending for deposit insurance activities (subfunction 373) and Treasury payments for interest on REFCORP bonds.

<sup>2</sup> Includes changes in the Federal Reserve surplus. A negative sign indicates a decrease in revenues.

**Deposit Insurance Funds.** Enacting H.R. 10 could affect the federal budget by causing changes in the government's spending for deposit insurance, but CBO has no clear basis for predicting the direction or the amount of such changes. Changes in spending for deposit insurance could be significant in some years, but would have little or no net impact on the budget over time.

Title III would convert to national banks all federal savings institutions in existence within two years of the date of enactment, thus allowing the merger of the BIF and SAIF. Both funds hold reserves in excess of the levels mandated by statute, and thus the combined fund would be well-capitalized initially. The SAIF insures far fewer and more geographically concentrated institutions than does the BIF, and those institutions focus on housing finance. A combined insurance fund thus could benefit from diversifying geographic and product risks that could lower the probability that the fund would become insolvent.

Other provisions in the bill could affect spending by the deposit insurance funds. Some are likely to reduce the risks of future bank failures. For example, H.R. 10 would permit affiliations of banking, securities, and insurance companies, thereby giving such institutions the opportunity to diversify and to compete more effectively with other financial businesses. Changes in the marketplace, particularly the effects of technology, have already helped to blur the distinctions among financial service firms. Further, regulatory and judicial rulings continue to erode many of the barriers separating different segments of the financial services industry. For example, banks now sell mutual funds and insurance to their customers and, under limited circumstances, may underwrite securities. At the same time, some securities firms offer checking-like accounts linked to mutual funds and extend credit directly to businesses. Because H.R. 10 would streamline the regulatory and legal structure that currently governs bank activities, CBO expects that its enactment would allow banks to compete more effectively in the rapidly evolving financial services industry. Diversifying income sources also could result in lower overall risks for banks, assuming that the expansion of their activities is accompanied by adequate safeguards. The bill would create "firewalls" to protect the banking components of a financial services organization from its riskier securities, insurance, or other financial activities, and would prohibit or limit certain transactions between banks and affiliates, hope-

fully preventing financial and informational abuses and conflicts of interest.

H.R. 10 also would allow banks to expand into relatively unfamiliar activities, thus possibly increasing the risk of bank failures. The bill would allow two approaches that would mix banking and commerce. Well-capitalized and healthy bank holding companies could own commercial firms as long as the aggregate commercial revenues do not exceed 15 percent of the holding company's gross domestic revenues. It also would allow a commercial firm to control a bank holding company with one small bank (less than \$500 million in assets). Similarly, revenues from the bank could not exceed 15 percent of the consolidated gross domestic revenues of the commercial firm.

But, permitting insured banks to diversify into product areas where they have little experience, or allowing commercial firms to own banks, raises questions about the adequacy of the regulators' ability to protect the insured entities and the insurance funds. Several federal banking regulators have expressed uncertainty about their ability to maintain adequate safeguards between the transactions of the insured institutions and their commercial affiliates and subsidiaries. A major concern would be preventing nonbanking losses in affiliates from draining the resources of the insured banks. To maintain safety and soundness in the banking system, H.R. 10 would specifically prohibit a bank from lending to a commercial affiliate and would impose a number of other restrictions. Nonetheless, experience with mixing commerce and banking in the United States has been limited. Ultimately, strong supervision and monitoring by regulators, which history has demonstrated is critical in limiting the exposure of the taxpayers during times of financial stress, would be essential to avoid additional losses to the deposit insurance fund.

If losses to the deposit insurance fund were to increase as a result of enacting H.R. 10, the BIF would increase premiums that banks pay for deposit insurance. Similarly, if losses were to decrease, banks might pay smaller premiums. As a result, the net budgetary impact is likely to be negligible over time in either case.

Conversion of Thrift Institutions. Two years after the date of enactment, all existing federal thrifts would be converted to national banks, and all state-chartered thrifts would be treated as state-chartered banks. At the same time, the OCC and the OTS would be merged, along with the bank and thrift deposit insurance funds, the BIF and the SAIF. Thrifts would no longer be required to maintain membership in the FHLB system. Finally, unitary thrift holding companies now in existence could continue to engage in all current activities, with certain limitations.

Merging the OTS and the OCC should result in long-term savings to the financial institutions that pay annual fees to cover the administrative expenses of the agencies. CBO estimates that reducing overhead and streamlining the examination process would result in cost savings of between \$10 million and \$15 million annually, once the merger is completed. The net budgetary effect of any such savings would be zero over time, however, because any reduction in expenses would result in a corresponding decrease in fee income.

Initially, CBO anticipates that the transition costs to move employees, to cover cancellations of leases, to train employees, to pay the costs of reductions-in-force, and to reprogram payroll, accounting, and other data systems, would cost about \$15 million over the 1999–2000 period. Based on information from the OTS and the OCC, we expect that the OTS would tap its existing reserve funds to pay these transition costs. Given the current OTS surplus, the agencies do not anticipate that fees paid by banks and the newly converted thrifts would be increased to replenish any reserves used for this purpose. As a result, CBO estimates that outlays would increase by \$8 million in 1999 and by \$7 million in 2000.

H.R. 10 would require about 1,100 federal thrifts to choose a new charter—either a state depository charter or a national bank charter. If no action is taken, the institution would automatically be designated a national bank. Under current law, the OCC is responsible for regulating national banks; the Federal Deposit Insurance Corporation (FDIC) regulates state-chartered banks that are not members of the Federal Reserve System; and the Federal Reserve regulates state-chartered member banks and bank holding companies. CBO expects that most thrifts would retain their state or federal affiliation, and that most large thrifts would become national banks, thus coming under the OCC's authority. The FDIC would supervise some smaller thrifts that shift their federal charters to either state thrift or state bank charters, as well as holding companies where the lead bank is state-chartered and not a member of the Federal Reserve System. We expect that abolishing the federal thrift charter would have a minimal effect of the supervisory activities of the Federal Reserve System. In addition, all the federal regulators are likely to have some additional examination activity associated with banks and nonfinancial affiliates.

As previously noted, with the exception of transition costs, transferring supervisory responsibility for newly chartered national banks from the OTS to the OCC would have no net budget effect, because both agencies charge fees to cover all their administrative costs. That is not the case with the FDIC, however, which uses deposit insurance premiums paid by all banks to cover the expenses it incurs to supervise state-chartered banks. Because the BIF and SAIF are well-capitalized, most banks and thrifts pay no premiums for deposit insurance at this time. Further, any increase in administrative costs triggered by H.R. 10 is not likely to result in future rate increases. CBO estimates that the FDIC would spend an additional \$2 million in 1998 and about \$18 million annually beginning in 1999 on regulatory and examination costs associated with its role in maintaining the safety and soundness of the institutions it supervises. CBO expects no significant administrative savings or costs from merging the BIF and the SAIF into a combined fund.

**Other Bank Regulatory Costs.** The Federal Reserve, the Securities and Exchange Commission (SEC), and state and federal banking regulators—the OCC, the FDIC, and the OTS—would have primary responsibility for monitoring compliance with the statute. The bill also would create a 10-member NCFS, headed by the Secretary of the Treasury, to determine what activities are financial in nature and which are not. It would have authority to issue regulations and to resolve disputes arising among providers of financial

services. CBO estimates that the NCFS would incur costs of \$2 million to \$3 million annually. These expenses would be shared by the member agencies and largely funded by fees paid by financial institutions or by agency appropriations.

In addition, the bill would impose consumer protection regulations governing retail sales of nondeposit products and other requirements. The banking agencies would be required to establish a consumer compliant mechanism to address various complaints, to develop programs for promoting housing finance, and to implement new regulations, policies, and training procedures related to securities, insurance and other areas. CBO expects that spending by the FDIC would total about \$1 million in 1998 and \$2 million annually for these new activities and for costs associated with monitoring compliance with the Community Reinvestment Act by the newly converted thrifts. The OCC and the OTS would also incur expenses for these purposes, but they would be offset by increased fees, resulting in no net change in outlays for those agencies.

Federal Home Loan Banks. The bill would make a number of reforms to the FHLB system, including: (1) Beginning in 1999, membership in the FHLB system would become voluntary; (2) total advances that the FHLBs could issue to institutions that do not qualify as thrift lenders would no longer be capped at 30 percent; and (3) investments could not exceed the amounts necessary to ensure liquidity, safety and soundness, and support for housing finance. H.R. 10 also would replace the \$300 million annual payment made by the FHLBs for the interest on bonds issued by the REFCORP with an assessment set at 20.75 percent of the FHLBs' net income.

Based on CBO's analysis of the FHLB system's balance sheet and income statement, and using economic assumptions consistent with the budget resolution baseline, CBO estimates that the FHLBs' net earnings will peak in 1998 at \$1.3 billion and gradually drop to about \$1.1 billion by 2002. As a result, CBO estimates that the provisions affecting the FHLBs would increase their payments to REFCORP by a total of \$44 million over the 1998–2002 period. The FHLB system is a government-sponsored enterprise and its activities are not included in the federal budget. But, because the Treasury pays the interest on REFCORP bonds not covered by the FHLBs, this change would reduce Treasury outlays by \$44 million over the five-year period.

Revenues. Based on information from the Federal Reserve, we estimate that H.R. 10 would require the Federal Reserve to incur added examination costs of about \$4 million per year once the bill's requirements are fully effective in 1999. These costs would be necessary to supervise the activities of the new bank holding companies as well as the new type of bank, the "woofie," which would not accept retail insured deposits. The Federal Reserve's cost of processing applications could also be affected. Applications for non-banking activities could decrease but applications for the newly authorized activities of holding companies could increase. We expect that these changes would be roughly offsetting, resulting in no net budgetary impact.

Because the Federal Reserve system remits its surplus to the Treasury, changes in its operating costs would affect governmental receipts. The net effect of the changes in this bill would be to re-

duce governmental receipts of \$17 million over the 1998–2002 period.

*Spending subject to appropriation*

A number of federal agencies would be responsible for monitoring changes resulting from enactment of H.R. 10. CBO estimates that total costs, assuming appropriation of the necessary amounts, would be about \$1 million in 1998 and \$3 million to \$4 million annually beginning in 1999, primarily for expenses of the SEC, the Treasury, and GAO. The SEC would incur costs to monitor market conditions, to examine firms, and to investigate practices to ensure compliance with the statute. The SEC would also be required to pay a portion of the annual expenses of the NCFs. We expect these additional rulemaking, inspection, and administrative expenses of the SEC would total less than \$1 million in 1998 and about \$2 million annually beginning in 1999. The Treasury also would participate in the NCFs, and we expect that its annual costs would be about \$1 million, once the NCFs is fully staffed and operating.

H.R. 10 would require GAO to conduct annual study evaluating competition in the financial services industry. CBS estimates that GAO would spend about \$1 million annual to collect and analyze data and prepare the report. Finally, DOJ would assume primary responsibility for streamlining the review of the antitrust implications of bank acquisitions and mergers. Based on information from DOJ, we expect that the department would continue to work with federal banking regulators to monitor such activity, and would incur no significant additional cost as a result of this change.

Pay-as-you-go considerations: Section 252 of the Balanced Budget and Emergency Deficit Control Act of 1985 sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. Legislation providing funding necessary to meet the deposit insurance commitment is excluded from these procedures. CBO believes that the various costs of H.R. 10 related to consumer protection and housing lending do not meet the exemption for the full funding of the deposit insurance commitment and thus would have pay-as-you-go implications. We estimate that direct spending changes resulting from the increase in the FDIC's supervisory costs associated with activities other than those related to safety and soundness would total about \$1 million in 1998 and \$2 million annually beginning in 1999. Costs for similar activities of the OCC and the OTS would be offset by increases in fees of an equal amount, resulting in no significant net budgetary impact for those agencies.

CBO estimates that provisions affecting the FHLBs would result in an increase in their payments for REFCORP interest and a corresponding decreasing in Treasury outlays, totaling \$109 million over the 1998–2007 period.

CBO expects that the Federal Reserve would incur additional expenses associated with consumer and housing issues that are not directly related to protecting the deposit insurance commitment. We estimate that the resulting increase in regulatory and other costs would reduce the surplus payment that the Federal Reserve remits to the Treasury by less than \$500,000 annually.

The net changes in outlays and governmental receipts that are subject to pay-as-you-go procedures are shown in the following

table. For the purposes of enforcing pay-as-you-go procedures, only the effects in the budget year and the succeeding four years are counted.

	By fiscal years, in millions of dollars—									
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Changes in outlays:										
FDIC .....	1	2	2	2	2	2	2	2	2	2
REFCORP payment .....	0	-22	-17	-4	-1	-1	-4	-11	-20	-29
Total .....	1	-20	-15	-12	-1	1	1	-2	-18	-27
Changes in receipts .....	0	0	0	0	0	0	0	0	0	0

Estimated impact on State, local and tribal governments: H.R. 10 contains several intergovernmental mandates as defined in UMRA. CBO estimates that the total cost complying with these mandates—primarily preemptions of state law—would be less than \$10 million a year. The bill contains other provisions, which are not mandates, but which CBO estimates would affect the budgets of state and local governments. H.R. 10 would not impose mandates or have other budgetary impacts on tribal governments.

#### *Mandates*

A number of provisions in H.R. 10 would preempt state banking and insurance laws. States would not be allowed to prevent banks from engaging in certain activities (such as selling insurance and securities) authorized under the act, nor would they be allowed to restrict the reorganization of mutual insurers. The bill would also allow federal bank regulators to enforce regulations that contradict state laws in certain circumstances. Such preemptions are mandates under UMRA. Based on information provided by the National Association of Insurance Commissioners (NAIC) and the Conference of State Bank Supervisors (CSBS), CBO estimates that enactment of these provisions would not result in direct costs or lost revenue to state governments because, while they would be prevented from enforcing certain rules and regulations, they would not be required to undertake any new activities.

Title IV of the bill would require a majority of states (within three years of enactment of H.R. 10) to enact uniform laws and regulations governing the licensing of individuals and entities authorized to sell insurance within the state. If a majority of states do not enact such laws, certain state insurance laws would be preempted and a National Association of Registered Agents and Brokers (NARAB) would be established. The purpose of the association would be to provide a mechanism through which uniform licensing, continuing education, and other qualifications could be adopted on a multistate basis. Membership in NARAB would be voluntary and open to any state-licensed insurance agent.

If NARAB is established, states would maintain the core functions of regulating insurance, such as licensing, supervising, and disciplining insurance agents and protecting purchasers of insurance from unfair trade practices, but certain state laws would be preempted. Specifically, Title IV would prevent states from discriminating against members of NARAB by charging different licensing fees based on residency and requiring compliance with

countersignature laws. Based on information from the NAIC about the number of out-of-state agents and current state license fees, CBO estimates that these preemptions would result in the loss of license fees to states totaling less than \$10 million a year.

Finally, the bill would require state regulatory agencies to make available certain reports to the Federal Reserve Board and to notify the board of any significant financial or operational risk to any depository institution from the activities of an affiliate of the institution. CBO estimates that the cost of complying with these requirements would not be significant.

#### *Other impacts*

Enactment of H.R. 10 would result in additional costs and revenues to state regulatory agencies. Certain provisions of the bill could lead to the establishment of new bank subsidiaries involved in insurance or securities activities. Because most states already allow banks to be involved in such activities, we expect that any additional costs would be small. In general, costs incurred by states would be offset by additional examination and licensing fees.

Title III also could result in additional workload for state banking agencies if federal thrifts whose charters are being abolished under the bill choose to become state-chartered financial institutions. Based on information from the CSBS, CBO estimates that any such increase in workload would be modest and that any costs would be offset by an increase in receipts from bank examination fees.

Finally, section 217 of the bill, which would expand the definition of "investment adviser" under the Investment Advisers Act, would increase the number of advisers registering with states, thereby increasing fee revenues. Based on information from the North American Securities Administrators Association (NASAA), CBO estimates that additional filing and registration fees would total approximately \$1 million annually.

Estimated impact on the private sector: H.R. 10 would impose several private-sector mandates as defined in UMRA. CBO's analysis of those mandates is contained in a separate statement of private-sector mandates.

Estimate prepared by: Federal costs: Mary Maginniss. Federal revenues: Mark Booth. Impact on State, local, and tribal governments: Marc Nicole.

Estimate approved by: Robert A. Sunshine, Deputy Assistant Director for Budget Analysis.

#### CONGRESSIONAL BUDGET OFFICE ESTIMATE OF COSTS OF PRIVATE-SECTOR MANDATES

#### *H.R. 10—Financial Services Competition Act of 1997*

Summary: Overall, H.R. 10 would reduce existing federal regulation of the financial services industry by relaxing restrictions on business and financial transactions throughout the economy. In particular, the bill would eliminate certain barriers to ties among banking organizations, other financial firms and commercial businesses. At the same time the bill would impose restrictions on newly authorized financial and commercial activities.

H.R. 10 would impose several new private-sector mandates as defined by the Unfunded Mandates Reform Act of 1995 (UMRA). The mandates identified in the bill would affect banking firms and other organizations that engage in financial activities. CBO estimates that the direct costs of those mandates would exceed the statutory threshold for private-sector mandates (\$100 million in 1996 dollars, adjusted annually for inflation) in 2003 because of requirements imposed on the Federal Home Loan Banks. Federally-chartered thrifts would probably experience some modest costs as a result of being forced to change charters within two years after enactment. The direct costs of mandates on banking organizations could be at least partially offset by savings from changes the bill would make to expand the powers of banks and bank holding companies.

Private-sector mandates contained in bill: H.R. 10 would impose new mandates on Federal Home Loan Banks (FHLBs), federal savings associations, and bank organizations. The largest costs are associated with mandates that would be imposed on the FHLB system. The primary mandates on FHLBs in the bill would require them to:

- Replace the \$300 million fixed annual payment for interest on Resolution Funding Corporation (REFCORP) bonds with a 20.75 percent annual assessment on net earnings; and

- Reduce the level of investments to the amount necessary for liquidity, safety and soundness, and housing finance.

The bill would also impose new mandates on federally-chartered thrifts (savings associations) and banking organizations. If enacted, major provisions in H.R. 10 would:

- Force all federally-chartered thrifts to convert to another charter within two years after enactment;

- Require banking organizations to adopt several consumer protection measures affecting sales of non deposit products;

- End the blanket exemption under the Securities Exchange Act of 1934 for brokers and dealers that conduct business in banks, making them subject to regulation by the Securities and Exchange Commission (SEC);

- End the exemption under the Investment Adviser Act of 1940 for bank investment advisers, making them subject to SEC examination and registration requirements; and

- End the authority of federally-charted banks (national banks) to sell title insurance directly in the bank.

Savings made possible by the bill could offset at least some of the costs of mandates in the bill. In particular, provisions that expand the allowable activities for banking organizations may lead to additional net income for these institutions as compared to current law.

Estimated direct cost to the private sector: The direct costs of private-sector mandates identified in this bill would exceed the threshold established in UMRA. Although mandates would become effective at different dates, CBO estimates that the aggregate costs of mandates would exceed the statutory threshold primarily due to mandates imposed on FHLBs. Under H.R. 10, CBO estimates that FHLBs would experience a reduction in net earnings as compared to projected net earnings under current law. In 2003, the fifth year after mandates on FHLBs would become effective, the estimated

loss in net earnings (direct costs) to FHLBs would rise to \$158 million. This amount exceeds the statutory threshold (\$100 million in 1996, adjusted annually for inflation) by about \$35 million dollars.

The direct costs of other mandates in the bill would not likely be significant. CBO estimates that the direct costs to federally-chartered thrifts of converting to another charter would amount to about \$14 million by the second year of enactment with zero costs thereafter. The direct costs of mandates on banking organizations for which we were able to obtain data would amount to less than \$11 million initially falling precipitously thereafter. Although data were not available for every mandate identified in the bill, the additional costs of these mandates are not expected to be expected to be significant.

The bill would also affect businesses and consumers in many ways other than through the mandates it contains. Estimates are more certain for the direct costs of mandates that are closely linked to legislative language. Greater uncertainty exists for the cost of mandates that are highly dependent on federal rulemaking. Moreover, there are many uncertainties concerning how firms might react to changes in financial and commercial markets as a result of provisions in this bill. The estimates provided below are of the direct costs (and potential savings) of mandates, and not the more general effects on the private sector. Where possible, a discussion of the broader effects is included.

#### *Federal Home Loan Bank reform*

H.R. 10 contains a number of provisions regarding the Federal Home Loan Bank (FHLB) system. The 12 Federal Home Loan Banks are private, member-owned institutions regulated by the Federal Housing Finance Board (FHFB). The FHLB system has more than 6,100 member institutions, including federal- and state-chartered thrift institutions, commercial banks, credit unions, and insurance companies. The FHLBs provide members with loans (advances) at attractive rates, and make investments in mortgage-backed securities and other financial assets. Members are required to purchase stock in the FHLBs; and the FHLBs pay dividends on that stock. Federal Home Loan Banks finance most of their assets through the sale of collateralized obligations. Because the FHLB system was created and chartered by the federal government, it is considered a government-sponsored enterprise, and its obligations are perceived to carry an implied federal guarantee. The implied guarantee enables the FHLBs to borrow funds from financial markets at low rates.

Many provisions of the bill would affect the administration of the Federal Home Loan Bank system. Section 177 of H.R. 10 would require each FHLB to submit for FHFB approval a capital structure plan and would authorize the FHFB to establish leverage and risk-based capital requirements for FHLBs. The bill would require two classes of FHLB stock with different voting and dividend features redeemable in either one or five years. Most banks surveyed by CBO are uncertain about how a new capital structure plan would affect operations, and hence, compliance costs.

Section 172A would require the Office of Finance, now a part of the FHFB, to become a part of the FHLB system. The Office of Fi-

nance issues consolidated obligations that are sold through investment firms and dealer banks or as direct placements. Banks are currently assessed a fee to cover the administrative costs of the Office of Finance; therefore, compliance costs are not expected to increase with this change. Section 172B of H.R. 10 would require 15 directors for each bank—9 elected and 6 appointed. Most banks currently have 15 or more directors; about 3 banks would have to hire an additional director. The cost of an additional director would vary by bank; fees plus expenses for a director usually range from \$22,000 to \$28,000.

Section 176 would replace the fixed annual payment made by FHLBs for the interest on Resolution Funding corporation (REFCORP) bonds with a 20.75 percent assessment on the net earnings of each FHLB. The bill would also allow an additional assessment allocated equally among FHLBs if necessary to meet the minimum REFCORP payment. FHLBs would no longer have to pay a fixed amount regardless of annual earnings; under H.R. 10 they would pay a fixed percentage of adjusted net earnings. CBO estimates that the new assessment rate would increase the payments made by FHLBs above the current payment of \$300 million annually by a total of \$45 million over the 1998–2003 period.

Section 178 would mandate that the FHLBs reduce the level of their investments to the amount necessary for liquidity purposes, or for safe and sound operation, or for housing finance. Depending on how regulators interpret this mandate, the earnings on investments could be lower as compared to those earned by FHLBs under current law. CBO assumes that the relevant provisions in this section would go into effect on January 1, 1999, and that the FHLBs would gradually reduce their holdings of mortgage-backed securities from 300 percent of capital in 1998 to 50 percent of capital by 2003. Money market and other financial investments were assumed to decline from 475 percent of total capital in 1998 to 150 percent by the year 2000. Those adjustments would bring the FHLBs investment portfolio close to the norm that was established before passage of the Financial Institutions Reform, Recovery and Enforcement Act of 1989.

Other provisions of the bill are likely to affect membership in the FHLB system and thereby could affect the earnings of FHLBs. Section 172 would repeal the federal mandate that requires federal savings associations to be members of the system effective January 1, 1999. (Most experts do not anticipate a large exodus of thrift institutions.) In addition, this section would allow community financial institution (defined as insured depository institutions with less than \$500 million in total assets) to be members in the Federal Home Loan Bank system by exempting them from the eligibility requirement that at least 10 percent of their total assets be in residential mortgage loans. This section of the bill would also allow community financial institutions that are members of the Federal Home Loan Bank system to get long-term advances for the purpose of funding small business, agriculture or rural development.

Allowing for the projected changes in investments and accounting for the effects of additional earnings from new members and the expanded possibility of earnings from advances. CBO estimates that net earnings to FHLBs (after payments for REFCORP and the

Affordable Housing Program) would be lower than net earnings projected under current law. The loss in net income would be counted as a direct cost of these mandates. The estimated cost to FHLBs, as measured by the loss in net income, increases from about \$30 million in 1999 to about \$122 million in 2002. By 2003, the fifth year after these provisions would become effective, the loss in net income totals \$158 million and would exceed the threshold for private-sector mandates under UMRA. Nonetheless, the returns to FHLB shareholders would remain above competitive levels, although by less than they would have been otherwise. CBO estimates that FHLBs' net earnings would peak in 1998 at \$1.3 billion, gradually drop to \$1.149 billion by 2002 and begin to rise again thereafter.

#### *Elimination of the Federal Thrift Charter*

Two years after enactment, Title III of the bill would require federal savings associations to automatically be converted by operation of law to national banks. The direct costs of this private-sector mandate are uncertain, but would not likely be significant. Moreover, the costs of regulating the newly converted banks would most likely be lower than under current law. If so, those savings would be passed on to regulated institutions.

The direct costs of conversion could include such items as conversion fees to a new chartering agency, the costs of replacing signs and stationery, the cost of a pre-conversion examination, and legal costs associated with adopting and conforming with the new charter. CBO assumes that the chartering agency would not charge federal savings associations a conversion fee and that the converting federal savings associations would not incur the legal costs associated with filing for conversion or the costs of a pre-conversion examination. Therefore, the direct costs of converting to a national bank would be the costs of replacing signs and stationery. Given that federal thrifts would have two years for this transition, new stationery would not necessarily be an additional cost. The cost to replace signs, assuming a cost of about \$2000 per branch, would amount to about \$14 million.

#### *Regulation of non-deposit products*

Section 112 of the bill would direct the federal banking agencies to adopt joint consumer protection regulations regarding bank retail sales of non-deposit products by any insured depository institution or any person engaged in such activities at an office of the institution or on behalf of the institution. The bill defines non-deposit products as investment and insurance products that are not deposit products as well as shares of registered investment companies. The major areas that must be addressed by regulation include:

Suitability standards—standards to ensure that an investment product sold to a consumer is suitable and any other non-deposit product is appropriate for a consumer based on financial information disclosed by the consumer;

Anti-coercion—a prohibition against engaging in any practices that would lead a consumer to believe that an extension of credit is conditional on the purchase of a non-deposit product from the institution or a subsidiary or affiliate;

Consumer disclosures—oral and written disclosures regarding the uninsured status of the product, the absence of a bank guarantee, possible changes in value and the prohibition on coercion in connection with a loan, and consumer acknowledgment of the receipt of such disclosures;

Physical segregation of activities—a requirement that retail deposits and transactions involving non-deposit products be conducted in separate settings, when possible; and

Sales personnel—a prohibition against the selling or offering of an opinion or investment advice on any non-deposit product by persons who are engaged in deposit taking functions; and standards allowing for such persons to make referrals to qualified persons only if the person making the referral receives no more than a one-time nominal fee for each referral that does not depend on whether the referral results in a transaction. Requirements regarding the qualifications of persons authorized to sell non-deposit products on behalf of an insured depository institution.

Currently, banks may engage in the retail sale of non-deposit products with some restrictions. National banks are allowed to engage in brokering (buying and selling) of all types of securities and investment products. State banks' securities activities vary from state to state, but most states permit state banks to engage in the sale of securities—currently, 43 states authorize discount or full securities brokerage, and 17 states allow banks to underwrite securities. Regarding insurance activities, permissible methods of entry for a bank generally depend on insurance powers granted under federal and state banking laws and state licensing requirements. A national bank may sell all lines of insurance as an agent, either directly or through a subsidiary, as long as it operates the insurance agency in towns with a population of 5,000 or less. Most states have laws that permit state bank sales of insurance either explicitly or implicitly through the operation of a “wild card” statute (permitting state banks to exercise the same powers as national banks).

Except for the anti-coercion provision, the provisions in section 112 are based on current industry guidelines issued in 1994 by bank regulators in an Interagency Statement on Retail Sales of Non-deposit Investment Products. The anti-coercion provision is similar to the anti-tying provision in current law. The consumer protection mandates would, depending on how regulators interpret these provisions, codify current industry guidelines and, therefore, would not likely impose measurable incremental costs on banks that currently engage in non-deposit activities.

*Additional regulator—National Council on Financial Services*

The bill would establish a new National Council on Financial Services to coordinate the regulation of financial services. The Council would include representatives from the Treasury Department (chair), the Federal Reserve Board (vice chair), the Federal Deposit Insurance Corporation (FDIC), Office of the Comptroller of the Currency (OCC), the Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission, two state in-

insurance regulators, a state securities regulator and a state banking regulator.

The bill would give the National Council on Financial Services the authority to prescribe additional, more stringent, consumer-related regulations if two years after the rules have been promulgated, the council decides that the regulations of the federal agencies are not sufficient to protect consumers. H.R. 10 also grants the council the authority to establish the regulatory framework that governs transactions and relationships between banks and their affiliates and subsidiaries. Because CBO has no basis for predicting the council's actions, we cannot estimate the costs of such potential incremental regulations on banks.

#### *Powers of national banks*

Although H.R. 10 would allow insurance agency and underwriting activities to be conducted by a bank affiliate under a bank holding company framework or by an insurance agency in a subsidiary of a bank, the bill would not expand insurance activities in the national bank itself. Instead, section 151 of the bill restates current law that prohibits insurance underwriting in a national bank and further provides that products being regulated by a state as insurance as of January 1, 1997, would be considered as insurance for purposes of the ban on insurance underwriting. That is, the bill would generally prohibit national banks from underwriting insurance except if they had OCC authorization to provide insurance as a principal as of January 1, 1997, or were already providing insurance as of that date. In determining if a new product after this date is insurance, a new administrative decision-making process would be created utilizing the National Council on Financial Services. A state insurance supervisory agency may petition the council to challenge an OCC determination regarding whether a new product (one not authorized or provided as of January 1, 1997) is an insurance product or a banking product. National banks would still be required to base insurance sales operations in towns with fewer than 5,000 people. CBO has no basis for predicting how regulators would define insurance products and therefore, we cannot estimate the costs of future restrictions on insurance activities.

Section 155 of the bill would end the current authority of national banks and their subsidiaries to sell title insurance as agent or principal. The direct costs of this prohibition, however, would be zero for existing institutions that sell title insurance because H.R. 10 would grandfather such institutions.

H.R. 10 would grant national bank organizations the authority to engage in new activities that would provide national banks with a potential new source of income. In particular, section 141 would authorize subsidiaries of national banks (with OCC approval) to engage in "financial activities" not allowed in the bank itself, except for merchant banking, insurance underwriting and real estate development. To engage in activities through a financial subsidiary, the national bank and all of its depository institution affiliates must be well capitalized, be well-managed and have at least a satisfactory rating under the Community Reinvestment Act (CRA). Examples of new activities for national bank subsidiaries include securities underwriting, and insurance agency activities not re-

stricted to small towns. In addition, section 151 of the bill would authorize national banks to underwrite municipal revenue bonds directly in the bank.

*Regulation of securities services and investment advisers*

Title II of H.R. 10 would amend the securities laws in order to provide functional regulation of existing and newly authorized bank securities activities. Under the bill, bank affiliates and subsidiaries would continue to be subject to the same regulation as other providers of securities products. However, banks engaging directly in securities activities, with certain exceptions (primarily related to traditional banking activities), would be required to register with the Securities and Exchange Commission. Also under the bill, bank employees involved in the sale of securities would be required to meet securities industry standards. Moreover, under H.R. 10, if a bank acts as an investment adviser to a registered investment company, the bank would be subject to the registration requirements and regulation under the Investment Adviser Act of 1940.

**Securities Services.** The Glass-Steagall Act generally prohibits banks from underwriting and dealing in securities, except for "bank-eligible" securities. Eligible securities are limited to those offered and backed by the federal government and federally-sponsored agencies, and certain state and local government securities. As banks have sought to expand their product lines, federal regulators have provided banks, through affiliated firms, limited authority to underwrite and deal in other types of securities. Generally, a firm that provides securities brokerage services (known as a broker-dealer) must register with and be regulated by the Securities and Exchange Commission and at least one self-regulatory organization such as the National Association of Securities Dealers (NASD), the New York Exchange, and the American Stock Exchange. Banks, however, are currently exempted from broker-dealer regulation.

H.R. 10 would end the current blanket exemption for banks from being treated as brokers or dealers under the Securities Exchange Act of 1934. Bank securities activities would, therefore, be subject to SEC regulation, with some exceptions. Sections 201 and 202 of the bill would exempt most traditional bank securities activities from registration and regulation as a broker-dealer under SEC regulation. The exemptions would cover many products that banks currently offer as agent so that these products would not trigger broker-dealer regulation. For example, private placements, trust activities, and U.S. government securities transactions would be exempt. Section 201 would also provide an exemption for broker-dealers that handle fewer than 1,000 securities transactions in a year. Moreover, the bill would not apply full broker-dealer regulation to those banks that would be required to register. Banks that register as brokers or dealers would not be required to become a member of the Securities Investor Protection Corporation (SIPC). Well-capitalized banks that register as brokers or dealers generally would not be subject to SEC net capital requirements.

According to the General Accounting Office, about 22 percent of banks offered securities brokerage services to their customers in

1994. The SEC and the National Association of Securities Dealers (NASD) regulated the securities activities of almost 90 percent of these 2,400 banks because they provided these services through registered broker-dealers or through third-party arrangements with registered broker-dealers. However, about 300 banks provided brokerage services on bank premises exclusively through bank employees. Those bank-direct brokerage operations were subject to regulation by federal bank regulators and were exempted from regulation by the SEC and NASD. Under H.R. 10, those 300 banks would potentially be subject to federal securities regulation. Many of these banks would probably be exempt, however, because they would not likely handle more than 1,000 transactions. Compliance costs of this mandate are, therefore, not likely to be large.

Banks affected by this mandate would have to register with the SEC and register with securities commissions in those states where they plan to do business. To register, a firm must provide the SEC with extensive amounts of information, including a list of its principals (individuals authorized to make transactions on behalf of a firm, such as investing or underwriting), a description of its planned business, any disciplinary history, criminal convictions, and a statement of financial condition. The information that must be supplied to the state is similar to that required by the SEC. The SEC has no registration fee; registration and required examination fees could vary from \$100 to \$600 by state depending on state requirements. As an upper bound estimate CBO assumed that all 300 banks would register in every state. Compliance costs for registration and examination would be less than \$9 million dollars.

Currently, any securities broker-dealer that wishes to do business with the public must become a member of the NASD and be subject to NASD regulation, examination and supervision. Under H.R. 10, banks that wish to continue brokerage services would also be required to become members of the NASD (and perhaps another other self-regulating organization in order to get a set on an exchange). NASD membership requirements for banks could include registering and certifying at least two principals, one of whom is designated as its financial and operating officer; written supervisory procedures to enable proper oversight of employee activities; business insurance (banks are typically bonded); a registered municipal principal for municipal business; a registered options principal for options activity; and a designated NASD executive representative who is the member's primary contact with the NASD. The cost of membership with the NASD depends on the level and types of securities services a firm decides to offer. Membership costs could range from \$2,500 to \$6,000 or more. In addition to the initial registration fees, banks would have to spend about \$400 annually on continuing education requirements for each registered person. The additional costs to banks to register with NASD would be less than \$2 million, assuming all 300 banks register.

New certification standards. Section 203 of the bill would require all bank employees involved in the sale of securities to be subject to the same rules applicable to employees of securities and other nonbank firms. Currently, over 90 percent of employees of banks that engage in securities transactions are already registered with the NASD and hence, comply with industry standards. Because

CBO has no basis for predicting how these provisions would be implemented, we cannot estimate the costs of such potential incremental regulations on banks. However, most industry experts surveyed by CBO expect the cost of complying with this mandate for the remaining portion of the industry would be relatively small.

**Investment Advisers.** Investment advisers are responsible for managing an investment portfolio in order to attain the greatest return consistent with the investment strategy established by the fund board of directors. The Investment Advisers Act requires that investment advisers register with the SEC; however, under current law banks acting as investment advisers to mutual funds are exempt from this requirement. Under this bill those companies would be required to register with the SEC as investment advisers and be subject to SEC regulation of this activity.

The Federal Reserve Board first authorized bank holding companies to act as investment advisers for mutual funds in 1972. Since that time banks have advised an increasing number of funds. Bank revenues from investment advisory activities were over \$900 million in 1994. In 1996, banks advised almost 3,000 mutual funds, representing about 30 percent of all funds registered with the Securities and Exchange Commission.

Currently, about 120 large bank holding companies engage in investment adviser activities. Before enactment of The National Securities Markets Improvement Act of 1996, the SEC charged a \$150 registration fee. Because of the 1996 act, the SEC is in the process of formulating a fee that will be based on the expected cost of administering the registration program, and the expected number of registrants. Banking organizations that continue to be investment advisers would have to pay this new registration fee annually and maintain books and records according to SEC rules. Inasmuch as the SEC is still in the very early stages of designing a system for registration, CBO has no basis to estimate the incremental costs of registering with the SEC. The costs, however, are not expected to be prohibitively large.

#### *Regulation of bank holding companies*

Section 133 of the bill would give statutory guidance to the Federal Reserve Board (FRB) regarding establishment of new capital rules or guidelines for bank holding companies. For example, the bill directs the FRB to take full account of the capital requirements imposed on non-depository institution subsidiaries by other federal or state regulatory authorities and of industry norms for capitalization of a company's unregulated subsidiaries and activities. The FRB would also be allowed to differentiate between different classes or categories of bank holding companies. Because it is uncertain how new capital rules would be implemented and, therefore, how they would affect operations, CBO has no basis for estimating compliance costs.

**Other private-sector effects:** H.R. 10 would dramatically overhaul federal regulation of the financial services industry. Provisions in this bill would potentially affect business and financial transactions throughout the U.S. economy. Major provisions of the bill would:

- Repeal key provisions of the Glass-Steagall Act, thereby allowing for the full integration of banking and securities firms;

Broadly expand the range of financial related activities that would be permissible for banking holding companies, including insurance underwriting;

Permit affiliations between bank holding companies and non-financial companies; and

Allow nonfinancial companies to acquire a bank, subject to certain asset size and revenue limitations.

*Qualified bank holding companies*

At the end of 1996, the number of bank holding companies totaled about 6,000. These organizations controlled over 7,000 insured commercial banks and held over 90 percent of the assets of all insured commercial banks. H.R. 10 would permit qualified bank holding companies (QBHCs), subject to certain safeguards, to engage in any financial activity. These activities would include a broad list of activities (including underwriting, dealing in, or making a market in securities and acting as a principal, agent or broker in connection with insurance or annuities) as well as any activity determined to be a financial activity by a newly established National Council on Financial Services. To be eligible to engage in new financial activities as a QBHC, all banks within a holding company must be well capitalized, well-managed and have at least a satisfactory rating under the Community Reinvestment Act. In addition, to be eligible banks must offer low-cost "life-line" checking accounts and they must be in compliance with the Fair Housing Act. QBHCs would be permitted to engage in any permissible activities without prior notice to the FRB. QBHC acquisitions of banks and bank holding companies would remain subject to FRB approval.

In addition to allowing banks, securities firms, and insurance firms to own each other, the bill would allow qualified bank holding companies to earn up to 15 percent of domestic gross revenues from investments in nonfinancial businesses such as manufacturing and retail sales. A QBHC's commercial activities within this 15 percent "basket" would be limited in that a QBHC could not become affiliated with any company which had consolidated assets at the time such affiliation occurs of more than \$750 million.

*Acquisitions of banks by commercial firms*

Section 106 of H.R. 10 would allow a commercial firm to acquire a single bank under certain conditions. A nonfinancial commercial firm would be permitted to derive up to 15 percent of domestic revenues from an investment in a bank that has assets of less than \$500 million. The bank must have been in business for at least five years at the time the bank is acquired, and must be held through an entity that is a QBHC. Any financial activities engaged in by such a commercial firm must be conducted through a subsidiary that the QBHC controls. A commercial firm that acquires a bank under this provision would not itself be treated as a bank holding company. The Federal Reserve would supervise nonfinancial holding companies that buy banks but only to the extent that activities may pose a potential risk to the federal safety net. Insurance companies in violation of the Fair Housing Act would not be permitted to affiliate with a bank.

*Nonbank banks*

The bill would lift current restrictions on cross-marketing and activities imposed on so-called nonbank banks. Nonbank banks are banks that before 1987 did not both accept demand deposits and make commercial loans. In 1987, Congress enacted the Competitive Equality Banking Act, which made such limited purpose banks subject to the Bank Holding Company Act in the future. However, existing limited purpose banks were grandfathered subject to certain restrictions, including a restriction that they could not engage in activities or lines of business that they were not engaged in as of March 5, 1987, and a restriction on the cross marketing of certain products. H.R. 10 would lift these restrictions.

*Wholesale financial institutions*

A commercial bank or securities company could establish or become an Investment Bank Holding Company to acquire or establish a Wholesale Financial Institution (“woofie”) which could not accept deposits that are insured or in initial amounts less than \$100,000. Woofies would have to comply with bank holding company restrictions and the Community Reinvestment Act. A holding company that owned a woofie but no federal insured depository institutions would be allowed greater flexibility (a larger basket) for non-financial investment.

*Mutual insurance companies*

The bill would permit mutual insurance companies to affiliate with banks if they move their home office to a state that allows mutual insurance companies to convert to a stock-owned company held by a mutual holding company.

*National Associations of Registered Agents and Brokers*

Title IV of the bill would require a majority of states (within three years of enactment of H.R. 10) to enact uniform laws and regulations governing the licensure of individuals and entities authorized to sell insurance within the state. If a majority of states do not enact such laws, section 402 of Title IV would establish the National Association of Registered Agents and Brokers (NARAB). The purpose of NARAB would be to provide a mechanism through which uniform licensing, continuing education, and other insurance producer qualifications could be adopted on a multi-state basis. If NARAB is established, states would maintain the core functions of insurance regulations such as licensing, supervising, and disciplining insurance producers and protecting insurance consumers from unfair trade practices, but certain state laws would be preempted. Specifically, Title IV would prevent states from discriminating against members of NARAB by charging different licensing fees based on residency and requiring compliance with countersignature laws.

Membership in NARAB would be voluntary and all state-licensed agents and brokers would be eligible, but NARAB would have the ability to establish its own membership criteria. Section 405 would give NARAB the authority to establish separate classes of membership, with separate criteria based on education, training, or experience required by different agent and broker duties. Membership in

NARAB would operate as licensure in each state in which the member pays the state licensing fee. NARAB would be funded solely through annual membership fees paid by agents and brokers who opt to become NARAB members.

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